Solution 26.1

a)

ESPRESSO LIMITED
NOTES TO THE FINANCIAL STATEMENTS

1. Accounting policies

1.1 Plant and equipment

Plant and equipment is stated in the statement of financial position at its revalued amount, being the fair value at the date of revaluation, less any subsequent accumulated depreciation and subsequent accumulated impairment losses. Revaluations are performed with sufficient regularity such that the carrying amounts do no differ materially from those that would be determined using fair values at the end of the reporting period.

The company has changed its accounting policy for plant. Previously plant was carried at cost less accumulated depreciation and impairment.

Depreciation is charged so as to write off the valuation of the plant and equipment over their estimated useful lives of eight years using the straight line method. The estimated useful lives, residual values and depreciation method are reviewed at each year end, with the effect of any changes in estimate accounted for on a prospective basis.

2. Plant

	C
Net carrying amount on 01/01/X6	150 000
Gross carrying amount	250 000
Accumulated depreciation	(100 000)
Revaluation	90 000
Depreciation	(30 000)
Net carrying amount on 31/12/X6	210 000
Gross carrying amount	240 000
Accumulated depreciation	(30 000)
Net carrying amount based on the cost model	131 250

3. Deferred taxation liability

		C
Temporary differences on plant & equipment	(29 000 + 26 100 + 5 800)	60 900

4. Change in estimate

The company changed the estimated useful life of the plant from ten years to twelve years. The effect of the change in estimate is as follows:

	C
- Current profits (before tax)	10 000
- Future profits (before tax)	(10 000)

Solution 26.1 continued …

b)

ESPRESSO LIMITED
STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 20X6

	Retained earnings	Revaluation surplus	Total
	R	**R**	**R**
Balance at 01 January 20X6	X	X	X
Total comprehensive income	X	63 900	X + 63 900
Transfer of realised portion	7 988	(7 988)	0
Balance at 31 December 20X6	X	55 912	X + 55 912

Workings

Deferred tax

		HCA	ACA	TB	TD	DT	RS	RE
01/01/X2	Cost		250 000	250 000				
01/01/X2 - 31/12/X5	Depreciation / tax allowances^		(100 000)	(200 000)				
31/12/X5	Balance	150 000	150 000	50 000	100 000	29 000		
01/01/X6	Revaluation		90 000	-	90 000	26 100	63 900	
		150 000	240 000					
01/01/X6 – 31/12/X6	Depreciation / tax allowances*	(18 750)	(30 000)	(50 000)	20 000	5 800		
	Transfer of realised surplus~						(7 988)	7 988
		131 250	210 000	0	210 000	60 900	55 912	

^ **Depreciation and tax allowances from 01/01/X2 – 31/12/X5**
- Depreciation = R250 000 X 0,10 X 4 yrs = R100 000
- Tax allowances = R250 000 X 0,20 X 4 yrs = R200 000

* **Depreciation and tax allowances from 01/01/X6 – 31/12/X6**
- HCA Depreciation = R150 000 / 8 yrs = R18 750
- ACA Depreciation = R240 000 / 8 yrs = R30 000
- Tax allowances = R250 000 X 0,20 = R50 000

~ Transfer of realised surplus
- R63 900 / 8 yrs or [(R30 000 – R18 750) X),71] = R7 988

Change in estimate

		Was	Is	Effect on current / future profits	
01/01/X6	Balance	150 000	150 000		
	Revaluation	90 000	90 000		
		240 000	240 000		
	Remaining useful life	*6 yrs*	*8 yrs*		
31/12/X6	Depreciation	(40 000)	(30 000)	10 000	Increase
		200 000	210 000		
Future periods	Depreciation	(200 000)	(210 000)	(10 000)	Decrease

Solution 26.2

a)

TECHNOWIZ LIMITED
STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 30 SEPTEMBER 20X8

	Note	Ordinary share capital C	Share premium account	Preference share capital C	Retained earnings C	Total
Balance at 1/10/20X7		750 000	622 500	200 000	126 200	1 698 700
Shares issued for cash	4	250 000	437 500			687 500
Total comprehensive income					163 373	151 623
Dividends - preference	5				(24 000)	(24 000)
ordinary	5				(70 000)	(70 000)
Balance at 30/9/20X8		1 000 000	1 060 000	200 000	195 573	2 455 573

Workings

* Stated capital		Qty A	C B	Premium B – A
Balance at 30/9/X7		***750 000***	***1 372 500***	
Rights issue	[1 for 3 (1 000 000 / 4)] (250 000 X C2,75)	250 000	687 500	622 500
Balance at 30/9/X8	(Given)	1 000 000	2 060 000	437 500

Profit		C
Gross profit		1 509 140
Operating expenses		(800 000)
Depreciation	(35 000 + 225 750 + 122 500)	(383 250)
Impairment		(26 000)
Adjustment to loss on sale of MV		~32 500
Interest	[(600 000 X 0,16 X 9/12) + (600 000 X 0,18 X 3/12)]	(99 000)
		233 390
Taxation	(28 042 + 41 975)	(70 017)
		163 373

~ Adjustment to loss on sale of MV		
Cost		60 000
Accumulated depreciation	(60 000 X 0,25 X 2 2/12)	(32 500)
Carrying amount		27 500
Proceeds		20 750
Loss		6 750
Recorded		39 250
Reverse		32 500

Tax computation		X 0,30
PBT	233 390	70 017 (Dr Tax E)
Temporary differences	139 917	41 975 (Cr D/T)
Depreciation	225 750	
Impairment	26 000	
Tax allowance	(391 667)	
Taxable profit	93 473	28 042 (Cr ROR)

STC (R94 000 X 0,125 = 11 750)

Solution 26.2 continued . .

a) continued …

The statement of financial position would appear as follows. It is shown here for completeness:

TECHNOWIZ LIMITED
STATEMENT OF FINANCIAL POSITION
AS AT 30 SEPTEMBER 20X8

	Note	C
ASSETS		
Non-current assets		3 171 500
Property, equipment and vehicles	8	3 078 500
Investments	9	93 000
Current assets		233 500
Inventory	10	68 750
Accounts receivable		51 200
Bank		113 550
		3 405 000
EQUITY AND LIABILITIES		
Share capital and reserves		2 455 573
Ordinary stated capital	4	1 000 000
Share Premium		1 060 000
12% Preference share capital	4	200 000
Retained earnings		195 573
Non-current liabilities		721 175
Loan from bank	6	600 000
Deferred tax	7	121 175
Current liabilities		228 252
Accounts payable		49 210
Interest payable		99 000
Current tax payable ^		28 042
Shareholders for dividends		52 000
		3 405 000

Solution 26.2 continued

b)

TECHNOWIZ LIMITED
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 30 SEPTEMBER 20X8

1. Accounting policies

1.1 Statement of compliance

These financial statements have been prepared in accordance with the approved accounting standards as applicable in Pakistan. Approved accounting standards comprise of such International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board as notified under the Companies Ordinance, 1984, provisions of and directives issued under the Companies Ordinance, 1984. In case the requirements differ, the provisions or directives of the Companies Ordinance shall prevail.

1.2 Basis of preparation

The financial statements are prepared in accordance with the historical cost basis. These policies are consistent in all material respects with those applied in the previous year.

1.3 Property, plant and equipment

Property, plant and equipment are stated in the statement of financial position at cost less accumulated depreciation and any accumulated impairment losses. Depreciation is charged so as to write off the cost of assets over their estimated useful lives using the straight line method. The estimated useful lives, residual values and depreciation method are reviewed at each year end, with the effect of any changes in estimate accounted for on a prospective basis.

Land is not depreciated.
Buildings are depreciated on the straight line method at 2% p.a.
Plant and equipment is depreciated at 20% p.a. on the straight line method.
Motor vehicles are depreciated at 25% p.a. on the straight line method.

1.4 Inventory

Inventory is valued at the lower of cost or net realisable value. Cost is determined on the weighted average basis. Net realisable value represents the estimated selling price for inventories less all estimated costs of completion and costs necessary to make the sale.

1.5 Deferred tax

Deferred tax is provided using the balance sheet liability method, on all temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax assets are recognized for all deductible temporary differences, carry forward of unused tax assets and unused tax losses, to the extent that it is probable that the taxable profit will be available against which the deductible temporary differences, carry forward of unused tax assets and unused tax losses can be utilized.

The carrying amount of deferred tax asset is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the deferred income tax asset to be utilized.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realized or the liability is settled, based on the tax rate (and tax loss) that have been enacted or substantially enacted at the balance sheet date.

4. Share capital

Authorised:

1 200 000 ordinary shares of no par value
400 000 12% preference shares of C0,50 each

Issued:

	Ordinary stated capital	**Preference share capital**
Number of shares in issue 1 October 20X7	750 000	400 000
Number of shares issued during the year	250 000	-
Number of shares in issue 30 September 20X8	1 000 000	400 000

The directors have unconditional authority until the next AGM to issue the remaining unissued shares of the company.

5. Dividends

Paid (12 000+30 000)	42 000
Declared (12 000+40 000)	52 000
	94 000

Solution 26.2 continued . .

b) continued …

6. Non-current liability

Secured:	
Loan from bank	600 000

The loan bears interest at prime less 2%, payable on 1 October each year, and is repayable on 30 September 20Y1. The loan is secured over land with a carrying value of R850 000.

7. Deferred tax liability

Deferred tax comprises temporary differences resulting from:

• Property plant and equipment	121 175

8. Property, plant and equipment

		Land	Buildings	Equipment	Motor vehicles	Total
Cost						
1/10/X7	Balance	850 000	1 750 000	990 000	470 000	4 060 000
	Additions			185 000	120 000	305 000
	Disposal				(60 000)	(60 000)
30/9/X8	Balance	850 000	175 000	1 175 000	530 000	4 305 000
Accumulated depreciation						
1/10/X7	Balance		218 750	396 000	235 000	849 750
	Depreciation		35 000	225 750	122 500	383 250
	Impairment			26 000		26 000
	Disposal				(32 500)	(32 500)
30/9/X8	Balance		253 750	647 750	325 000	1 226 500
	Carrying amount	850 000	1 496 250	527 250	205 000	3 078 500

Land and buildings comprise a factory situated on stand 674 Edenvale township.

Cost of land 1 September 20X0	850 000
Factory 30 June 20X1	1 750 000
	2 600 000

An impairment loss has been recognised during the year for equipment. The equipment's recoverable amount of R40 000 is its net selling price that declined significantly due to major technological advances in this type of machinery.

9. Investment in subsidiary

Unlisted:		
Investment in Data (Pvt) Ltd	30 000 ordinary shares	60 000
Loan to Data (Pvt) Ltd		33 000
		93 000
Directors valuation of investment		60 000

Solution 26.2 continued . .

b) continued …

10. Inventory

Inventory comprises:	
Raw materials	15 150
Work-in-progress	12 600
Finished goods	41 000
	68 750

Finished goods with a carrying amount of R36 000 are carried at net realisable value.

Workings

Equipment: opening cost: (1 175 000 – 185 000)
Equipment: depreciation: (990 000 X 0,20) + (185 000 X 0,20 X 0,75)
Motor vehicles: opening cost: (530 000 – 120 000 + 60 000)
Motor vehicles: depreciation [(530 000 - 120 000) X 0,25] + [60 000 X 0,25 X 2/12] + [120 000 X 0,25 X 7/12]
Buildings: depreciation: 1 750 000 X 0,02

Deferred tax on equipment

		CA	TB	TD	DT
30/9/X7	(^990 000 – 396 000) (990 000 – *660 000)	594 000	330 000	264 000	79 200
Purchase		185 000	185 000	-	-
Depreciation W&T	(198 000 + 27 750) (330 000 + 61 667)	(225 750)	391 667	165 917	(49 775)
Impairment	(66 000 – 40 000)	(26 000)	-	(26 000)	(7 800)
30/9/X8		527 250	123 333	403 917	121 175

^ (1 175 000 – 185 000)

* (990 000 x 0.20 = 198 000 . . . .Equipment two years old . . .990 000 x 0.33 x 2yrs = 660 000)

Solution 26.3

a)

General Journal		Debit	Credit
Plant: accumulated depreciation		60 000	
Plant: cost			60 000
Set-off of acc depreciation against cost (NRVM)			
Plant: cost		10 000	
Revaluation surplus			10 000
Revaluation of plant			
Revaluation surplus		3 000	
Deferred tax			3 000
Deferred tax on revaluation surplus			
Depreciation		12 500	
Plant: accumulated depreciation			12 500
Depreciation on plant			
Revaluation surplus	*(10 000 x 70%)/ 4 yrs*	1 750	
Retained earnings			1 750
Transfer from revaluation surplus to retained earnings			
Depreciation		25 000	
Buildings: accumulated depreciation			25 000
Depreciation on plant			
Buildings: accumulated depreciation	*200 000 – 60 000*	140 000	
Buildings: cost			200 000
Bank		300 000	
Profit on sale			240 000
Sale of a building			
Telephone expenses		20 000	
Telephone prepaid			20 000
Expensing of prepaid telephone expense			
Bank		15 000	
Rental income received in advance			15 000
Rental income received in advance as at 31 December 20X6			
Deferred tax	*(750 + 3 000 + 6 000 + 6 000 + 4 500)*	20 250	
Tax expense			20 250
Deferred tax adjustment for 20X6			

Solution 26.3 continued …

b)

TISSOT LIMITED
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 20X6

		C
8. Deferred taxation asset/ (liability)		
The deferred tax balance comprises temporary differences caused by:		
• Property, plant and equipment	*Given*	30 750
• Year-end accruals	*(0 + 4 500)*	4 500
		35 250
Reconciliation		
Opening balance	*24 000 – 6 000*	18 000
Deferred tax on revaluation surplus	*Given*	(3 000)
Deferred tax in statement of comprehensive income	*Balancing or per journal*	20 250
Closing balance	*30 750 + 4 500*	35 250
9. Property, plant and equipment		
Property, plant and equipment comprises:		
• Plant	*40 000 + 10 000 – 12 500*	37 500
• Buildings	*360 000 – 25 000 – 60 000*	275 000
		312 500
Reconciliation: plant		
Net carrying amount – 1 January	*Given*	40 000
Gross carrying amount – 1 January	*Given*	100 000
Accumulated depreciation – 1 January	*Given*	(60 000)
Revaluation surplus	*Given*	10 000
Depreciation	*Given*	(12 500)
Net carrying amount – 31 December	*Balancing*	37 500
Gross carrying amount – 31 December	*100 000 – 60 000 + 10 000*	50 000
Accumulated depreciation – 31 December	*Given*	(12 500)

Plant is measured using the revaluation model, with revaluations recorded using the net replacement value method. Plant is revalued every three years, with the last revaluation performed on 1 January 20X6 by an independent sworn appraiser and member of the institute of valuers in Pakistan. Had the cost model been applied instead, the carrying amounts would have been as follows:

Net carrying amount – 31 December	*(CA: 40 000 – 40 000 / RUL: 4 years)*	30 000
Reconciliation: buildings		
Net carrying amount – 1 January	*Given*	360 000
Gross carrying amount	*Given*	500 000
Accumulated depreciation	*Given*	(140 000)
Depreciation	*Given*	(25 000)
Sale	*Given*	(60 000)
Net carrying amount – 31 December	*Balancing*	275 000
Gross carrying amount	*500 000 – 200 000*	300 000
Accumulated depreciation	*140 000 + 25 000 – (200 000 – 60 000)*	(25 000)

Solution 26.3 continued …

c)

TISSOT LIMITED
STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 31 DECEMBER 20X6

	Share capital C	Revaluation surplus C	Retained earnings C	Total C
Balance – 1 January 20X6	210 000	0	235 000	445 000
Total comprehensive income		^7 000	197 000	204 000
Transfer to retained earnings		(1 750)	1 750	0
Dividends declared			(17 000)	(17 000)
Balance – 31 December 20X6	210 000	5 250	416 750	632 000

^ (10 000 – 3 000)

Solution 26.4

a)

WODEN LIMITED
STATEMENT OF COMPREHENSIVE INCOME
FOR THE YEAR ENDED 28 FEBRUARY 20X2

		C
Profit before interest and tax		263 763
Finance cost	(50 000 + 5 763 [W1])	(55 763)
Profit before tax		208 000
Income tax expense	(62 400 [W2/1] + 2 900 [W2/2])	(65 300)
Profit for the period		142 700
Other comprehensive income		
Revaluation surplus		280 000
Total comprehensive income		422 700
Earnings per share	(R142 700 – 21 000 [W5] / 159 000 [W3])	0.765

W1 Effective interest		C
Premium	(3 634 X 6/12)	1 817
Discount	(1 817 X 6/12)	909
(Accrual of premium and amortisation of discount for 01/03/X1 - 31/08/X1)		
Premium	(4 050 X 6/12)	2 025
Discount	(2 025 X 6/12)	1 012
(Accrual of premium and amortisation of discount for 01/09/X1 - 28/02/X2)		
		5 763

W2.1 Tax computation	C	C	
Profit before tax	208 000	62 400	Dr Tax expense
Temporary differences	(100 000)	30 000	Cr Deferred tax
- Depreciation	150 000		
- Tax allowance	(250 000)		
Taxable income	108 000	32 400	Cr ROR

W2.2 Underprovision	C
Assessment for 20X1 year	30 200
Provided for 20X1 year	(27 300)
Under provision	2 900

W3 EPS

		Total		20X2	20X1
28/02/X1	Balance	100 000		100 000	100 000
31/05/X1	Cash issue (on preference share redemption)	8 000	(9/12)	6 000	-
		108 000		106 000	100 000
28/02/X2	Capitalisation issue	54 000		53 000	50 000
		162 000		159 000	150 000

Solution 26.4 continued . .

b)

WODEN LIMITED
STATEMENT OF CHANGES IN EQUITY FOR THE PERIOD ENDED 28 FEBRUARY 20X2

	Ordinary share capital	Share premium	Preference share capital	Revaluation surplus	Retained earnings	Total
Balance	1 000 000	20 000	400 000		610 450	2 030 450
Issue of shares	80 000	8 000				88 000
Preference shares redeemed [W4]		(7 500)	(300 000)			(307 500)
Share issue expenses		(4 000)				(4 000)
Capitalisation issue [W5]	540 000	(16 500)			(523 500)	
Preference dividend [W6]					(21 000)	(21 000)
Total comprehensive income				*280 000	142 700	422 700
	1 620 000	-	100 000	280 000	208 650	2 208 650

* Dr Land & Buildings	400 000	
Cr Revaluation surplus		280 000
Cr Deferred tax		120 000

W4 Capitalisation issue

Number of shares before capitalisation issue	(W3)	108 000
		C
Capitalisation issue	(54 000 X R10)	540 000
- Share premium	(20 000 + 8 000 - 7 500- 4 000)	(16 500)
. . Retained earningss		***523 500***

W5 Preference dividend

		C
Dividend on preference shares redeemed	(300 000 X 0,12 X 3/12)	9 000
Dividend on remaining preference shares	(100 000 X 0,12 X 12/12)	12 000
		21 000

Solution 26.4 continued . .

c)

WODEN LIMITED
NOTES TO THE FINANCIAL STATEMEMENTS
AT 28 FEBRUARY 20X2

1 Accounting policies *(not required)*

1.1 Statement of compliance

These financial statements have been prepared in accordance with the approved accounting standards as applicable in Pakistan. Approved accounting standards comprise of such International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board as are notified under the Companies Ordinance, 198, provisions of and directives issued by under the Companies Ordinance, 1984. In case the requirements differ, the provisions or directives of the Companies Ordinance, 1984 shall prevail.

1.2 Basis of preparation

The financial statements have been prepared on the historical cost basis, except for the revaluation of the property. These policies are consistent in all material respects with those applied in the previous year.

1.3 Property, plant and equipment

Property, plant and equipment is stated at cost less accumulated depreciation and any accumulated impairment losses. Depreciation is charged so as to write off the cost of assets over their estimated useful lives using the straight line method. The estimated useful lives, residual values and depreciation method are reviewed at each year end, with the effect of any changes in estimate accounted for on a prospective basis.

Land and buildings are depreciated. Plant and equipment is depreciated at 20% per annum on the straight line basis.

1.4 Deferred tax

Deferred tax is provided using the balance sheet liability method, on all the temporary differences at the balance sheet date between the tax base of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax asset are recognized for all deductible temporary differences, carry forward of unused tax losses, to the extent that is probable that future taxable profit will be available against which the deductible temporary difference, unused tax losses and tax credits can be utilized.

Carrying amount of deferred tax asset is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that the related tax benefit will be realized. Deferred taxis calculated at the rates that are expected to apply to the period when differences reverse based on the tax rates and tax laws that have been enacted or substantively enacted by the balance sheet date.

2. Taxation	**C**
Normal tax	
- Current tax	32 400
- Deferred tax	30 000
- Under-provision prior year	2 900
Income tax expense	65 300

Tax rate reconciliation	**%**	**C**
Tax expense on profit / applicable rate	30.0	62 400
- Under-provision prior year	1.4	2 900
Tax expense / effective rate	31.4	65 300

3. Deferred taxation	**C**
Temporary differences on plant and equipment	60 000
Revaluation of property	120 000
	180 000

Solution 26.4 continued . .

c) continued …

4..Earnings per share

The calculation of earnings per share is based on basic earnings as shown below and on the weighted average number of ordinary shares in issue of 159 000 (20X1 : 150 000)

The calculation of the weighted average number of shares is after a cash issue on 31 May as well as a capitalisation issue on 28 February 20X2. Comparatives have been restated accordingly.

Reconciliation of earnings with profit for the period

Profit for the period	142 700
Preference dividend	(21 000)
Basic earnings	121 700

5. Share capital *(not required)*

	C
Authorised	
200 000 ordinary shares of R10 each	2 000 000
50 000 12% redeemable preference shares of R10 each	500 000
Issued	
162 000 ordinary shares of R10 each	
10 000 12% redeemable preference shares of R10 each	

	Ordinary shares	Preference shares
Number of shares in issue at 28/02/X1	100 000	40 000
Preference shares redeemed		(30 000)
Shares issued for cash	8 000	
Capitalisation issue	54 000	
Number of shares in issue at 28/02/X2	162 000	10 000

The redeemable preference shares are redeemable on 30 May 20X5 at the option of the company.

6. Non-distributable reserve

Revaluation surplus on property	200 000

7. 10% Debentures

50 000 10% debentures of R10 each		500 000
Premium on redemption	[9 821 (at 31/08/01) + 2 025 (4 050 X 6/12)]	11 846
Discount on issue	[20 090 (at 31/08/01) – 1 012 (2 225 X 6/12)]	(19 078)
		492 768

The debentures are secured over the fixed property of the company and are redeemable at a premium of 10% on 30 August 20X8.

Solution 26.4 continued . .

c) continued …

8. Property, plant and equipment

	Property	Plant and equipment	Total
Cost / Revaluation			
Balance at 28/02/X1	2 200 000	750 000	2 950 000
Revaluation	(600 000)	-	(600 000)
	400 000		400 000
Balance at 28/02/X2	2 000 000	750 000	2 750 000
Accumulated depreciation			
Balance at 28/02/X1	400 000	150 000	550 000
Depreciation expense	200 000	150 000	350 000
Revaluation	(600 000)	-	(600 000)
Balance at 28/02/X2	-	300 000	300 000
Carrying amount	2 000 000	450 000	2 450 000

Land and buildings were revalued at the end of the current year by an independent valuer.

9. Post reporting period event

A dividend of C0,10 per share, amounting to R16 200 was declared on 21 March 20X2 in respect of the year ending 28 February 20X2

W7

Taxation expense			
Description	***C***	***Description***	***C***
ROR	2 900	Retained earnings	65 300
Deferred Tax / ROR	62 400		
	65 300		65 300

Receiver of Revenue			
Description	***C***	***Description***	***C***
Balance	1 200	Tax expense	2 900
Bank	1 700		
Bank	14 700	Tax expense	32 400
Bank	15 300		
Balance	3 000		
	35 300		35 300
		Balance	3 000

Deferred tax

	Carrying amount	Tax base	Temporary difference	Deferred tax	
01/03/X0	750 000	750 000			
28/02/X1	(150 000)	(250 000)	100 000	30 000	Cr
	600 000	500 000	100 000	30 000	Cr
28/02/X2	(150 000)	(250 000)	100 000	30 000	
	450 000	250 000	200 000	60 000	Cr

Solution 26.5

COULTREAD CARS LIMITED
STATEMENT OF COMPREHENSIVE INCOME
FOR THE YEAR ENDED 31 MARCH 20X1

		C
Profit before taxation	(398 600 - 10 500 - 127 500 -34 875 + 119 500 + 250 000)	595 225
Taxation	(99 068 + 1 500)	(100 567)
Profit for the period		494 658
Other comprehensive income		0
Total comprehensive income		494 658

COULTREAD CARS LIMITED
STATEMENT OF FINANCIAL POSITION AS AT 30 MARCH 20X1

		C
ASSETS		
Non-current assets		
Property, plant and equipment		177 625
EQUITY AND LIABILITIES		
Non-current liabilities		
Deferred tax	[53 288 – 625 (5 000 X 0,125)]	53 288
Current liabilities		
Receiver of Revenue		59 055

COULTREAD CARS LIMITED
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 30 MARCH 20X1

1. Accounting policies

1.1 Statement of compliance
These financial statements have been prepared in accordance with the approved accounting standards as applicable in Pakistan. Approved accounting standards comprise of such International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board as are notified under the Companies Ordinance, 198, provisions of and directives issued by under the Companies Ordinance, 1984. In case the requirements differ, the provisions or directives of the Companies Ordinance, 1984 shall prevail.

1.2 Basis of preparation
The financial statements have been prepared on the historical cost basis. These policies are consistent in all material respects with those applied in the previous year.

1.3 Property, plant and equipment
Property, plant and equipment is stated at cost less accumulated depreciation and any accumulated impairment losses. Depreciation is charged so as to write off the cost of assets over their estimated useful lives using the straight line method. The estimated useful lives, residual values and depreciation method are reviewed at each year end, with the effect of any changes in estimate accounted for on a prospective basis.

Plant and machinery is depreciated at 15% p.a. on the straight-line basis.

1.4 Deferred tax
Deferred tax is provided using the balance sheet liability method, on all the temporary differences at the balance sheet date between the tax base of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax asset are recognized for all deductible temporary differences, carry forward of unused tax losses, to the extent that is probable that future taxable profit will be available against which the deductible temporary difference, unused tax losses and tax credits can be utilized.

Carrying amount of deferred tax asset is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that the related tax benefit will be realized. Deferred taxis calculated at the rates that are expected to apply to the period when differences reverse based on the tax rates and tax laws that have been enacted or substantively enacted by the balance sheet date.

Solution 26.5 continued . . .

2. Profit before tax includes:

		C
Depreciation	- Factory buildings	10 500
	- Plant and machinery	127 500
Impairment loss on plant and machinery		34 875
Profit on expropriation on land and factory buildings (250 000 + 119 500)		369 500

3. Taxation

Normal Tax	
Current tax	110 955
Deferred tax	(11 888)
Under provision in prior year	1 500
Income tax expense	100 567

No secondary tax on companies is payable due to an STC credit of C5 000 available for set-off in the future.

Tax reconciliation		**C**	**%**
Tax effect at applicable rate on profit before tax	(595 225 X 0.3)	178 568	30.00
Tax effect of:			
Permanent differences	(265 000 X 0.3)	(79 500)	(13.36)
Under provision		1 500	0.25
Tax expense/ effective rate		100 568	16.89

4. Property, plant and equipment

	Plant and machinery C	**Land C**	**Factory buildings C**	**Total C**
Cost				
Balance 31/3/20X0	850 000	400 000	630 000	1 880 000
Expropriation		(400 000)	(630 000)	1 030 000
Balance 31/3/20X1	850 000	-	-	850 000
Accumulated depreciation				
Balance 31/3/20X0	510 000	-	189 000	699 000
Depreciation	127 500	-	10 500	138 000
Impairment loss	34 875	-		34 875
Expropriation			(199 500)	(199 500)
Balance 31/3/20X1	672 375	-	-	672 375
Carrying amount	177 625	-	-	177 625

The impairment loss of R34 875 results from plant and machinery becoming obsolete. The recoverable amount is based on the net selling price of the scrap value.

Solution 26.5 continued . .

Workings

W1 Factory buildings			Carrying amount	Tax base
1/10/19X2	Cost		630 000	630 000
31/3/20X0	Accumulated depreciation / Tax allowance	(630 000 / 25 X 7,5) (630 000 X 0,05 X 7,5)	(189 000)	(236 250)
			441 000	393 750
31/8/20X0	Depreciation	(630 000 / 25 X 5/12) (630 000 X 0,05 X 5/12)	(10 500)	(13 125)
			430 500	380 625
	Expropriation proceeds		550 000	550 000
	Profit/ recoupment		119 500	169 375

W2 Plant and machinery			Carrying amount	Tax base
	Cost		850 000	850 000
31/3/20X0	Accumulated depreciation / Tax allowances	(Given) / (850 000 X 0,20 X *4)	(510 000)	(680 000)
			340 000	170 000
31/3/20X1	Depreciation	(850 000 X 0,15) / (850 000 X 0,20)	(127 500)	(170 000)
			212 500	-
	Impairment	(212 500 / 4 = 53 125) (53 125 - 18 250)	(34 875)	
			177 625	-

* (850 000 X 0,15 = 127 500 . . . 510 000 / 127 500 = 4 years at beginning of year)

W3 Deferred tax calculation	Carrying amount	Tax base	Temporary difference	Deferred tax	
Factory buildings					
31/3/20X0	441 000	393 750	47 250	14 175.00	Cr
	(10 500)	(13 125)	2 625	787.50	Cr
31/8/20X0	430 500	380 625	49 875	14 962.50	Cr
Expropriation	(430 500)	(380 625)	(49 875)	^(14 96250)	Dr
After Expropriation	0	0	0	0.00	
Plant & machinery					
31/3/20X0	340 000	170 000	170 000	51 000.00	Cr
	(127 500)	(170 000)			
	(34 875)		7 625	^2 287.50	Cr
31/3/20X1	177 625	0	177 625	53 287.50	Cr

^ (14 962,50 – 2 287,50 = net 11 888 Dr to deferred tax)

Solution 26.5 continued . .

W4 Profit before tax

Profit before depreciation and tax		398 600
Depreciation – factory building		(10 500)
– plant and machinery		(127 500)
– impairment loss		(34 875)
Profit on expropriation of factory buildings		119 500
Profit on expropriation of land	(650 000 – 400 000)	250 000
		595 225

W5 Tax computation			**X 0.30**	
Profit before tax		595 225		
Permanent difference				
Dividends received		(15 000)		
Profit on expropriation of land		(250 000)		
		330 225	99 068	Dr T/E
Temporary differences		39 625	11 888	Dr D/T
Depreciation / impairment	(10 500 + 127 500 + 34 875)	172 875		
Tax allowances	(13 125 + 170 000)	(183 125)		
Accounting gain on expropriation of factory buildings (W1)		(119 500)		
Tax gain on expropriation of factory builing		169 375		
Taxable profit		369 850	110 955	Cr CTP

W6 Underprovision / amount owing

Per assessment	51 900	51 900
Per statement of comprehensive income 31/3/X0 / Provisional payents	50 400	46 000
Under provision / Amount owing	1 500	5 900

CURRENT TAX PAYABLE

Description	C	Description	C
Bank (3rd)	5 900	Balance	4 400
Bank (1st)	23 000	Under provision	1 500
Bank (2nd)	28 900	Tax expense	110 955
Balance	59 055		
	116 855		116 855

DEFERRED TAX

Description	C	Description	C
Tax expense	11 888	Balance	65 175
Balance	53 287		
	65 175		65 175
		Balance	53 287

Solution 26.6

ACE OF SPADES (PRIVATE) LIMITED
STATEMENT OF COMPREHENSIVE INCOME
FOR THE YEAR ENDED 31 MARCH 20X9

	Note	20X9	20X8
		C	C
Profit before tax	2	376 400	568 500
Income tax expense	3	(130 105)	(193 725)
Profit for the period		246 295	374 775
Other comprehensive income		0	0
Total comprehensive income		246 295	374 775

ACE SPADES (PRIVATE) LIMITED
EXTRACT FROM STATEMENT OF FINANCIAL POSITION
AS AT 31 MARCH 20X9

	20X9	20X8
ASSETS	C	C
Non-current assets		
Property, plant and equipment	796 500	504 000
Current assets		
Tax receivable	15 745	-
EQUITY AND LIABILITIES		
Non-current liabilities		
Deferred taxation	89 775	92 400
Current liabilities		
Shareholders for dividends	90 000	-
Tax payable	-	3 500

Solution 26.6 continued …

ACE SPADES (PRIVATE) LIMITED
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 MARCH 20X9

1. Accounting policies

1.1 Statement of compliance
These financial statements have been prepared in accordance with the approved accounting standards as applicable in Pakistan. Approved accounting standards comprise of such International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board as are notified under the Companies Ordinance, 198, provisions of and directives issued by under the Companies Ordinance, 1984. In case the requirements differ, the provisions or directives of the Companies Ordinance, 1984 shall prevail.

1.2 Basis of preparation
The financial statements have been prepared on the historical cost basis. These policies are consistent in all material respects with those applied in the previous year.

1.3 Deferred tax
Deferred tax is provided using the balance sheet liability method, on all the temporary differences at the balance sheet date between the tax base of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax asset are recognized for all deductible temporary differences, carry forward of unused tax losses, to the extent that is probable that future taxable profit will be available against which the deductible temporary difference, unused tax losses and tax credits can be utilized.

Carrying amount of deferred tax asset is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that the related tax benefit will be realized. Deferred taxis calculated at the rates that are expected to apply to the period when differences reverse based on the tax rates and tax laws that have been enacted or substantively enacted by the balance sheet date.

2. Profit before tax

Profit before tax includes

	20X9	**20X8**
	C	**C**
Depreciation	133 500	144 000
Loss of plant and machinery due to earthquake (tax saving: R134 400)	(384 000)	

3. Taxation

		20X9	**20X8**
		C	**C**
Normal tax			
• Current tax	20X9: W1 and 20X8: 193 725 – 33 600	127 855	160 125
• Deferred tax	20X9: W3/ W1 & 20X8: 92 400 – 58 800	(2 625)	33 600
• Under provision prior year	20X9: W4 & 20X8: assumed	4 875	0
Tax expense		130 105	193 725

Tax rate reconciliation

	20X9		**20X8**	
	C	**%**	**C**	**%**
Tax at applicable rate	131 740	35.0	198 975	35.0
Exempt income	(6 510)	(1.7)	x	x

Under provision prior year	4 875	1.3	-	-
Per statement of comprehensive income / effective rate	130 105	34.6	193 725	34.1

x = Not enough information available.

Solution 26.6 continued …

4. Deferred tax asset/ (liability)

Deferred tax liability	**20X9**
	C
Property, plant and equipment	89 775

Workings

W1 Tax computation

	20X9	**X 0.35**	
	C		
Profit before tax	376 400		
Permanent difference			
Dividends received	(18 600)		
	357 800	125 230	Dr Tax expense
Temporary differences	7 500	2 625	Dr Deferred tax
Depreciation (120 + 13.5)	133 500		
Tax allowance (240 + 270)	(510 000)		
Loss on plant destroyed	384 000		
Taxable profit	365 300	127 855	Cr CTP

W2 Balance owing to taxation authorities

CURRENT TAX PAYABLE			
Description	***C***	***Description***	***C***
Bank	8 375	Balance	3 500
Bank	84 250	Taxation (under-provision)	4 875
Bank	59 350	Taxation	127 855
		Balance	15 745
	151 975		151 975
Balance	15 745		

Solution 26.6 continued …

W3 Deferred tax:

	Carrying amount	Tax base	Temporary difference	Deferred tax
Old plant				
Opening balance	0	0	0	0
Purchase	720 000	720 000	0	0
Depreciation/ wear & tear (6/12)	(72 000)	(240 000)	(168 000)	(58 800)
31/3/X7	648 000	480 000	(168 000)	(58 800)
Depreciation/ wear & tear	(144 000)	(240 000)	(96 000)	(33 600)
31/3/X8	504 000	240 000	(264 000)	(92 400)
Depreciation/ wear & tear (10/12)	(120 000)	(240 000)		(42 000)
Before plant destroyed	384 000	-	(384 000)	(134 400)
Impairment loss	(384 000)		384 000	134 400
After plant destroyed	-	-	-	-
New plant				
1/3/20X9	810 000	810 000	-	-
Depreciation/wear & tear (1/12)	(13 500)	(270 000)	(256 500)	(89 775)
31/3/X9	796 500	540 000	(256 500)	(89 775)

W4 Under provision:

Tax expense X8	given	193 725
Deferred tax charge X8	(92 400 – 58 800)	(33 600)
Current tax provided for in X8		160 125
Current tax per assessment X8	given	(165 000)
Under provision		(4 875)

Solution 26.7

a) Journals

	Debit	Credit
Year ended 31 December 20X1:		
1 July 20X1		
Cost: nuclear plant – physical structure (80%)	6 400 000	
Cost: nuclear plant – major inspection (20%)	1 600 000	
Bank/ liability		8 000 000
Purchase of nuclear plant: 20% relates to 20X1 inspection		
1 July 20X1		
Cost: nuclear plant – dismantling costs	453 942	
Provision for future dismantling costs		453 942
Purchase of nuclear plant: 20% relates to 20X1 inspection		
31 December 20X1		
Finance costs	27 237	
Provision for future dismantling costs		27 237
Notional finance charges due to the unwinding of the discount: 12% x 453 942 x 6/12 (or see W1)		
31 December 20X1		
Depreciation - nuclear plant (expense)	1 178 727	
Accumulated depreciation: nuclear plant – physical structure		600 000
Accumulated depreciation: nuclear plant – major inspection		533 333
Accumulated depreciation: nuclear plant – dismantling costs		45 394
Depreciation of nuclear plant components:		
physical structure = (6 400 000 – 400 000) / 5 years x 6/12		
major inspection = (1 600 000 – 0) / 18 months x 6 months		
dismantling costs = (453 942 – 0) / 5 years x 6/12		
Year ended 31 December 20X2:		
1 July 20X2		
Repairs and maintenance (expense) (60%)	300 000	
Cost: nuclear plant – new part (40%)	200 000	
Bank/ liability		500 000
Repair of central shaft (60%) and fitment of new part (40%) that increases future economic benefits		
31 December 20X2		
Finance costs	57 742	
Provision for future dismantling costs		57 742
Notional finance charges due to the unwinding of the discount: (453 942 + 27 237) x 12%; or see W1: 27 237 + 30 505		
31 December 20X2		
Depreciation - nuclear plant (expense)	2 382 455	
Accumulated depreciation: nuclear plant – physical structure		1 200 000
Accumulated depreciation: nuclear plant – major inspection		1 066 667
Accumulated depreciation: nuclear plant – dismantling costs		90 788
Accumulated depreciation: nuclear plant – new part		25 000
Depreciation of nuclear plant components:		
physical structure = (6 400 000 – 400 000) / 5 years		
major inspection = (1 600 000 – 0) / 18 months x 12 months		
dismantling costs = (453 942 – 0) / 5 years		
new part = (200 000 – 0) / 4 years x 6/12		

Solution 26.7 continued …

a) Journals continued …

	Debit	Credit
Year ended 31 December 20X3:		
2 January 20X3		
Cost: nuclear plant major inspection	1 500 000	
Bank/ liability		1 500 000
Major inspection on 2 January 20X3		
2 January 20X3		
Accumulated depreciation: nuclear plant – major inspection	1 600 000	
Cost: nuclear plant major inspection		1 600 000
Derecognition of 20X1 major inspection (carrying amount: nil)		
31 December 20X3		
Finance costs	64 670	
Provision for future dismantling costs		64 670
Notional finance charges due to the unwinding of the discount:		
(453 942 + 27 237 +57 742) x 12%; or see W1: 30 505 + 34 165		
31 December 20X3		
Depreciation - nuclear plant (expense)	2 090 788	
Accumulated depreciation: nuclear plant – physical structure		1 200 000
Accumulated depreciation: nuclear plant – major inspection		750 000
Accumulated depreciation: nuclear plant – dismantling costs		90 788
Accumulated depreciation: nuclear plant – new part		50 000
Depreciation of nuclear plant components:		
physical structure = (6 400 000 – 400 000) / 5 years		
major inspection = (1 500 000 – 0) / 2 years		
dismantling costs = (453 942 – 0) / 5 years		
new part = (200 000 – 0) / 4 years		

Comments:

- Although there are 2 years between each major inspection, there are only 18 months left on the cost of the 20X1 inspection until the next inspection (as at the date of the purchase of the nuclear plant: 1 July 20X1). Therefore, the remaining useful life of the 20X1 major inspection is 18 months.
- The useful life of the future dismantling cost is dictated by the date of the future dismantling (30 June 20X6) together with the date on which the asset became available for use (1 July 20X1): 60 months or 5 years.
- Part of the repair invoice relates to the purchase of a new part that results in an increase in expected future economic benefits through a 20% increase in the power supply and should therefore be capitalised.
- Although the new part (installed on 1 July 20X2) has the same remaining useful life as the original physical structure to which it has been fitted, its cost is significant and should therefore be recognised as a separate component. On the date of fitment, the nuclear plant structure – and therefore the new part – has a remaining useful life of 4 years (until the date of dismantling).
- Notice that the major inspection is fully depreciated by 31 December 20X2. If there had been a balance on this account on the date of the next major inspection, the remaining carrying amount would first have had to be written off before capitalisation of the next inspection. Do, however, remember that even if the carrying amount is C0, (as in this case), the cost and accumulated depreciation must still be reversed (derecognised).
- Notice that the cost of the dismantling (part of the nuclear plant asset) does not change as time goes by, but rather the provision for dismantling costs (the liability) changes: increases with the notional interest caused by the 'unwinding of the discount'.

Solution 26.7 continued …

b) Disclosure

BLUE TIDE LTD
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 20X3

4 Property, plant and equipment

	20X3	20X2	20X1
Total net carrying amount:	**C**	**C**	**C**
Other assets listed per classification	xxx	xxx	xxx
Nuclear plant	4 501 972	5 092 760	7 275 215
	xxx	xxx	xxx

Nuclear plant			
Net carrying amount: 1 January	5 092 760	7 275 215	0
Gross carrying amount:	8 653 942	8 453 942	0
Accumulated depreciation and impairment losses:	(3 561 182)	(1 178 727)	0
Additions	1 500 000	200 000	8 453 942
Depreciation	(2 090 788)	(2 382 455)	(1 178 727)
Net carrying amount: 31 December	4 501 972	5 092 760	7 275 215
Gross carrying amount: *(20X3: 8 653 942 – 1 600 000 + 1 500 000)*	8 553 942	8 653 942	8 453 942
Accumulated depreciation and impairment losses: *(20X3: 3 561 182 – 1 600 000 + 2 090 788)*	(4 051 970)	(3 561 182)	(1 178 727)

Workings

W1 Present value table: future dismantling costs (the entire table is not required)

Date	O/balance	Finance costs	Obligation	C/balance
1 July 20X1	0		453 942	
31 December 20X1	453 942	27 237		481 179
31 July 20X2		27 237		508 415
notional interest – first 12 month period		54 473		
31 December 20X2	508 415	30 505		538 920
31 July 20X3		30 505		569 425
notional interest – second 12 month period		61 010		
31 December 20X3	569 425	34 165		603 590
31 July 20X4		34 165		637 756
notional interest – third 12 month period		68 331		
31 December 20X4	637 756	38 265		676 021
31 July 20X5		38 265		714 287
notional interest – fourth 12 month period		76 531		
31 December 20X5	714 287	42 857		757 144
31 July 20X6		42 857		800 001
notional interest – fifth 12 month period		85 714		
difference due to rounding		(1)		(1)
				800 000
Total notional finance costs		346 058		